BEFORE THE
UNITED STATES DEPARTMENT OF AGRICULTURE
WASHINGTON, D.C.

NAVEL ORANGES GROWN IN ARIZONA AND DESIGNATED PART OF CALIFORNIA; PROPOSED WEEKLY LEVELS OF VOLUME REGULATION FOR THE 1991-92 SEASON

Docket No. FV-91-408PR

COMMENTS OF THE DEPARTMENT OF JUSTICE

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By notice dated September 30, 1991, the United States Department of Agriculture ("USDA") requested comments on the need to regulate the quantity of fresh California-Arizona navel oranges in the 1991-92 season. The Navel Orange Administrative Committee, a group composed of competing area growers and handlers, has proposed for the 1991-92 season a cartel-like arrangement to reduce output by limiting the volume of fresh navel oranges that may be shipped; this is effectuated by a weekly shipping schedule and weekly percentage allocations among districts. This recommendation by a group of entities that should be competitors has been published by USDA as a proposed rule. 56 Fed. Reg. 49432.

<u>POSITION OF THE DEPARTMENT OF JUSTICE</u>

Volume regulation or "prorate" of California-Arizona navel oranges in the 1991-92 season should not be adopted by the Secretary of Agriculture. While volume regulation is unlikely ever to further the objectives of the Agricultural Marketing Agreement Act of 1937 ("AMAA" or "the Act"), such regulation would be particularly harmful and costly in a season with a smaller crop such as now forecast by USDA for 1991-92.

Volume regulation imposes clear net costs on society. Prorate has increased prices of domestic fresh navel oranges above the level that would have prevailed in the absence of volume regulation and has thereby induced wasteful production of navel oranges. Ironically, however, prorate has not increased long-run grower returns above what growers would have received absent volume regulation. Moreover, it is not clear that prorate provides any price stabilization benefits, let alone benefits sufficient to outweigh the consumer and misallocation costs it engenders. On the contrary, there is strong evidence that prorate is harmful. During seasons when prorate was suspended the net social welfare of growers and consumers increased. Indeed, the effects of the December 1990 freeze illustrate how this misguided and costly regulation serves only to exacerbate the negative effects on both growers and consumers of uncontrollable natural events.

DISCUSSION

I. The Statutory Basis for the Proposed Rule

The proposed rule has been issued under Marketing Order No. 907 (7 C.F.R. § part 907), as amended.1/ The Order authorizes regulation of the handling of navel oranges grown in Arizona and designated parts of California. The Order and any rules issued pursuant to it will bind all handlers, including those who do not wish to participate in the Order. Thus, the proposed rule, if adopted by the Secretary, will impose mandatory restraints on the quantity of fresh navel oranges that may lawfully be marketed domestically in fresh form by all orange growers in Arizona and designated parts of California.2/

Pursuant to the Order, on June 25, 1991, the Navel Orange Administrative Committee ("NOAC") adopted a marketing policy on which the proposed rule is based. The proposed rule would limit the quantity of fresh navel oranges that California and

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1/ The Secretary of Agriculture is empowered by the Agricultural Marketing Agreement Act of 1937, as amended, 7 U.S.C. §§ 601 et seq. ("AMAA"), to regulate the handling of a broad range of agricultural commodities. Under the AMAA, the Secretary of Agriculture is authorized to issue marketing orders, which are regulations that govern the activities of all specified handlers of a particular product.

2/ Indeed, the Act contains sanctions, both criminal and civil, that may be imposed upon handlers who do not adhere to the regulations. See, 7 U.S.C. § 608(c)(J)(14).

Arizona handlers may sell to American consumers in the 1991-92 navel orange season.3/

The Secretary cannot implement the proposed rule unless he determines that such action is likely to promote the policies of the AMAA. 7 U.S.C. §§ 608(c)(4), 608 (c)(16)(A). Among those policies is the achievement of parity prices for commodities covered under the Act. 7 U.S.C. §§ 602(1) and (2). The policy of particular relevance to the proposed rule is that found in Section 602 (4) of the Act, which states:

It is declared to be the policy of Congress --

> [T]o establish and maintain such orderly marketing conditions . . . as will provide, in the interests of producers and consumers, an orderly flow and supply [of the particular product] to market throughout its normal marketing season to avoid unreasonable fluctuations in supplies and prices.4/

3/ NOAC estimated the total navel orange crop in the coming season and each individual handler's share of that total. NOAC has also recommended a schedule that specifies for each week of the season the maximum quantity of fresh navel oranges that the industry may make available to American consumers; that schedule is the centerpiece of the proposed rule. During each week covered by the schedule, an individual navel orange handler may not market domestically a quantity in excess of its prorate share of the weekly maximum for the industry. (Though a handler may exceed its prorate share in any given week, that amount is subject to a payback later.) Thus, handlers' ability to manage their sales volumes is constrained by industry-wide decisions over which they have little control.

4/ The proposed rule restates this policy goal of the Act and further states that limiting the quantity of California-Arizona navel oranges that each handler may handle on a weekly basis may contribute to the Act's objectives. 56 Fed. Reg. at 49432.

Courts generally have recognized protection of the purchasing power of farmers as a central aspect of the Act.5/ The language of the statute, however, also expressly directs the Secretary to temper the objective of enhancing grower income with the requirement that the interests of consumers also be taken into account.6/ The statute plainly states, the goal of "orderly marketing conditions" is to benefit both producers and consumers. 7 U.S.C. § 602(4).7/

In order to protect consumers, the rate of adjustments in prices [to achieve parity] must be compatible with the "public interest." 7 U.S.C. § 602(2). Competitive considerations, including the efficient allocation of resources, generally are

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5/ See, e.g., Stark V. Wickard, 321 U.S. 288, 302 (1944); United States v. Rock Royal Co-op, 307 U.S. 533, 550 (1939); Rasmussen v. Hardin, 461 F.2d 595, 599 (9th Cir. 1972), cert. denied, 409 U.S. 933 (1972).

6/ The Secretary of Agriculture, in determining "crucial facts and conclusions . . . cannot be guided solely by deference to industry desires." Walter Holm & Co. v. Hardin, 449 F.2d 1009, 1016 (D.C. Cir. 1971); Fairmont Foods Co. v. Hardin, 442 F.2d 762, 766 (D.C. Cir. 1971).

7/ Neither NOAC nor USDA has attempted to define "orderly marketing conditions" for purposes of the navel orange marketing order. In its response to comments filed with respect to proposed volume regulation for the 1990-91 navel orange season, USDA appeared to equate the avoidance of unreasonable fluctuations in supplies and prices with orderly marketing conditions. 55 Fed. Reg. 50162. In our dynamic and growing economy, adaptation and growth are qualities to be encouraged. It is not clear at what point normal and healthy price and supply fluctuations are considered by NOAC or USDA to be "unreasonable" or harmful.

considered to be an important element of the public interest standard, which qualifies not only this program, but also many other types of federal economic regulatory programs.8/ Accordingly, the Secretary has identified the maximization of producer returns within the context of open and competitive marketing and the achievement of a more efficient allocation of resources as important goals in administering fruit and vegetable marketing orders. See USDA, Guidelines for Fruit, Vegetable and Specialty Crop Marketing Orders (1982). Economic principles as well as past experience strongly indicate that the proposed rule will frustrate rather than effectuate the goals set forth both by the Secretary and the Act itself.

II. Prorate for Navel Oranges Is Not in the Public Interest

The notice of proposed rule states that the major reason for the use of volume regulations under the navel orange marketing order is "to establish and maintain orderly marketing conditions for navel oranges and thereby benefit producers through higher returns." 56 Fed. Reg. 49432. The notice suggests that "Such regulation can at the same time benefit consumers by maintaining adequate supplies of navel oranges in the marketplace during the season." Id. The Marketing Policy

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8/ See, e.g., United States v. FCC, 652 F.2d 72, 88 (D.C. Cir. 1980); Sabin v. Butz, 515 F.2d 1061, 1069 (10th Cir. 1975); Cities of Statesville v. AEC, 441 F.2d 962, 987 (D.C. Cir. 1969); Northern Natural Gas Co. v. FPC, 399 F.2d 953, 959 (D.C. Cir. 1968).

Statement of the Navel Orange Administrative Committee ("Policy Statement") contains numerous conclusory statements asserting the benefits of the program, but provides no factual basis for concluding that implementing either volume or size controls in the California-Arizona navel orange industry in the 1991-92 season, would best serve the interests of producers and consumers.9/ Indeed, available evidence suggests the contrary -- prorate has resulted in an increase in the proportion of the crop used for less-valued purposes, and recent suspensions of volume regulation in navel oranges have not resulted in "disorder" or other harm. Economic theory would predict, and experience confirms, that any financial benefit to producers from volume regulation is likely to be temporary and clearly outweighed by the continued harm to consumers and a wasteful misallocation of society's resources.

A. Prorate Harms Consumers in the Short and Long Run

Volume controls in the navel orange industry are based on recommendations of the NOAC. The Committee specifies the maximum quantity of navel oranges handlers may ship fresh during a given week. In effect, NOAC acts as a legalized cartel to set output for navel oranges. Production in excess

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9/ The proposed rule indicates that while size regulation is not now being advocated by the NOAC, it seeks authority to impose such regulation at a later date. Size regulations have the same harmful effects as prorate and the analysis contained in these comments applies equally to that type of regulation.

of the allowed quantity must be held for shipment at a later time, be processed, exported or left on the tree.10/

Consumers are hurt in the short and long run by higher prices caused by prorate. In the short run, because of the higher prices, some consumers do not buy fresh navel oranges or buy fewer navel oranges than they would otherwise. These consumers are forced by prorate to forego purchasing fresh navel oranges at the lower prices that would exist in a free market. The navel orange consumption foregone is a clear economic loss. In the long run, there is overproduction of navel oranges because prorate temporarily increases returns, leading to entry or expansion of production. This increased production, however, does not yield a net benefit to consumers, because, as explained below, a substantial proportion is inefficiently diverted to the low-valued processing market or left to rot. On the contrary, consumers are hurt by navel orange overproduction encouraged by prorate. Scarce resources, including land and water, are spent to produce a product --

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10/ NOAC's Policy Statement (at 19) notes that navel oranges may be stored on the tree even after they reach maturity. NOAC's conclusion is that such storability makes volume regulation more appropriate. This is incorrect. The greater the ability to store a commodity the better able are growers and handlers to maximize their profits by releasing their product to the market in response to price signals. Unregulated oranges would not be rushed to market; navel orange growers and handlers, like other unregulated marketers, would control the flow of their product to purchasers in an efficient manner.

California-Arizona navel oranges used for processing or fed to cattle -- not justified by the value placed upon it by consumers.11/ Consumers would be better off if these resources were used for producing goods of greater value to consumers, including fresh navel oranges.

B. Prorate Creates Significant Resource Misallocation

The Committee has expressed concern about the "boom and bust cycle in perishables."12/ Presumably NOAC is concerned that periods of short supplies and high prices will lead to periods of abundant supplies and low prices and that that cycle will continue to repeat itself unless there is regulation to even it out. USDA, in its notice of final rule on volume regulation of navel oranges in the 1990-91 season (55 Fed. Reg. 50164, December 5, 1990), also expressed concern about "gluts" on the market. Gluts are situations where there is so much product on the market that prices are less than production costs. Shortages are situations where there is so little product that prices are far greater than production costs. Gluts and shortages both reflect the economic cost of a market disequilibrium, but in general a free market will cope with

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11/ The NOAC Policy Statement (at 8) notes the serious water shortage as a continuing concern of agriculture in California.

12/ Policy Statement at 13.

these problems more efficiently than regulation by the government or a private cartel.13/

The mere fact that gluts and shortages may occur occasionally (because of weather or other factors) is not a sufficient basis for imposing a far-reaching regulatory scheme. Such regulation as prorate can be justified only after consideration of whether the purported benefits of the regulation can be achieved by reliance on market forces. As demonstrated in Section D, however, the benefits of price stabilization and orderly marketing can be, and are, accomplished in unregulated markets through a variety of mechanisms available to navel orange growers and handlers.

Of equal importance is the fact that the current regulatory scheme imposes the very costs it seeks to avoid by, in effect, producing chronic shortages (in fresh product use) and gluts (in surplus product uses) simultaneously. Under the current regulatory program, NOAC decides what fraction of the navel oranges grown will be sold in the domestic fresh market. The remainder of the crop must then be exported, processed or fed

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13/ Gluts demonstrate a waste of resources since more was spent to produce a product than the product will be worth to buyers. Shortages represent a wasted opportunity. Consumers would have valued additional production at more than the cost of providing it, so the socially valuable opportunity to provide that added production is wasted. Even if gluts and shortages occur at the same time, as when there is a glut in one location and a shortage in another location, the same principle applies: gluts and shortages are inefficient.

to cattle. Such regulation causes high prices and shortages in the domestic fresh market and low prices and gluts of oranges for processing.

This regulatory waste can be quantified. Growing oranges costs, on average, $2,292 per acre and there are 123,000 acres of California-Arizona navel oranges in production.14/ Total production cost is thus $282 million, without taking into account the cost of picking and marketing the oranges. Since processing gives growers virtually no on-tree returns, i.e., the cost of picking and marketing the oranges, by itself, exceeds the price that growers can obtain from processors,15/ and since the demand for processed oranges is very elastic,16/ navel oranges diverted to processing provide no net value to society. Thus, each percent of the crop that is processed as a result of regulation is a net waste of $2.82 million of

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14/ See, USDA Economic Research Service Report No. 650, "Cost of Producing Oranges," June 1991 at 6; and NOAC Policy Statement Table D.

15/ USDA, Fruit and Tree Nuts Situation and Outlook Report Yearbook, August 1991, at 51.

16/ P.K. Thor and E.V. Jesse, Economic Effects of Terminating Federal Marketing Orders for California-Arizona Oranges, USDA, Economic Research Service Technical Bulletin No. 1664, 1981, 21. See also, N. Powers, G. Zepp and F. Hoff, Assessment of a Marketing Order Prorate Suspension: A Study of California-Arizona Navel Oranges (USDA Agricultural Economic Report 557) (1986) at 19.

production costs. And this does not include the waste attributable to foregone consumption.

The fraction of the crop that was processed grew from 7 percent in 1960 (averaging 20 percent in the 1960s) to one-quarter of the crop in the 1980s.17/ Under normal weather conditions about 11 percent of the crop is actually unsuitable for fresh sale.18/ Thus, we have been wasting 14 percent of the crop (25 percent less 11 percent). That translates to $40 million in wasted production costs on an annual basis over the last decade.19/ Producers in unregulated markets try to supply the market without waste or shortages, and they succeed a good deal of the time. Since the actual effect of prorate is to create gluts and shortages (in processing and fresh navels,

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17/ NOAC Policy Statement, Fox Table 1.

18/ Thor and Jesse, in their 1981 study (at 29-30), supra, n. 16, state that 90% of the navel oranges from districts 1 and 3 are suitable for fresh sale, as are 85% of the navel oranges from district 2. NOAC Policy Statement Table E shows that in the 1980s production was distributed among the districts as follows: district 1, 86%; district 2, 11%; district 3, 2%; and district 4, 1%. Even if none of the oranges in district 4 can be sold fresh, 89% of all oranges produced can be sold fresh.

19/ For the 1991-92 crop, the Committee forecasts that it will allow 69% of the crop to be sold fresh, expects that 12% of the crop will be exported, and that 17% of the crop will be processed. The remainder will go to charitable or other unregulated uses. Given the analysis provided above, i.e., assuming that 11 percent of the crop will not be suitable for fresh sale, under the predictions made by NOAC, prorate would result in $17 million of waste in the 1991-92 season.

respectively), and thereby to create waste, it seems clear that the preferable solution would be less, not more, regulation.

C. Growers Receive No Long Run Benefits from Prorate

The navel orange prorate can enhance grower revenue only in the short run.20/ The prorate can raise revenue in the short run by suppressing the volume of sales permitted from a given level of fresh navel orange production, but the prorate does not preclude new entry into navel orange production or expansion by existing producers. Any artificially raised returns to navel orange growers will provide incentives for new navel orange production and thus the supracompetitive grower returns will not persist. Increased production from new entry or expansion means that increasingly larger quantities of fresh navel oranges would have to be diverted to processing, exports or to cattle feed over time in order to maintain artificially high fresh prices.

20/ Prorate restrains sales of fresh oranges. Such restraints raise grower revenue in the short run if the demand for fresh navel oranges is relatively inelastic, as compared to demand in the processing market. When demand is relatively inelastic, a given percentage reduction in output generates a larger percentage increase in price. Conversely, when demand is relatively elastic, a given percentage expansion in output generates a smaller percentage decrease in price. Thus, by diverting otherwise merchantable fresh navel oranges from the fresh to the processing market, in the short run prorate may increase prices and grower revenue more in the fresh market than it decreases prices and revenue in the processing market. Overall, average returns to growers may thereby increase in the short run relative to returns attainable in a market not subject to volume regulation.

Increased diversion to the processing market lowers weighted average returns and, as these returns are distributed over a larger volume of production, average returns per acre decline. Inevitably, weighted average returns seek the point where they equal the long-run costs of production and growers earn only a normal return on their investment. While the long-run return is only the normal competitive market return, prorate-caused diversion imposes short- and long-run costs on consumers -- higher prices and lower output of fresh navel oranges, and foregone alternative uses of acreage devoted to unwanted navel orange growing.

The available empirical evidence supports the conclusion that growers do not receive increased long-run returns from prorates. Shepard's 1986 study of the California-Arizona orange industry,21/ and Smith's 1961 study of the lemon industry22/ both found that growers did not earn long-run returns above what they could have earned without volume regulation.

Many studies have found that the use of prorates results in an oversupply of total navel production as a result of the artificially high prices of fresh navel oranges that such

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21/ L. Shepard, Cartelization of the California-Arizona Orange Industry, 1934-1981, 29 J. of L. & Econ. 83 (1986).

22/ Smith, The Lemon Prorate in the Long Run, 69 J. of Pol. Econ. 573, (1961).

restrictions produce. In 1981, Thor and Jesse found there might be up to 30 percent excess production as a result of prorates.23/ Two studies, in 1986 and 1990, found that production had increased so much that the average on-tree returns for processed oranges were negative.24/

D. Price Stabilization Benefits of Prorate Are Speculative

Some advocates of prorate argue that it produces a societal benefit by lowering grower risk. This argument has two steps: First, prorate is alleged to reduce grower risk by constraining fresh sales during large crop years and second, to the extent that growers prefer to avoid or reduce risk, it is argued that they will tend to view the resulting reduction in risk as a reduction in their cost of production.25/ Such reductions in

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23/ Supra, n. 16.

24/ N. Powers, G. Zepp & F. Hoff, supra, n. 16, at 3; N. Powers, Effects of Marketing Order Prorate Suspension on California-Arizona Navel Oranges, 7 Agribusiness, 203, 214 (1990). See also, USDA Fruit and Tree Nuts Situation and Outlook Report Yearbook, supra, n. 15.

25/ This is the common argument that prorate provides stabilization benefits. In its Policy Statement at 16, NOAC has introduced a novel argument. NOAC describes the potential for "panic" sales by growers and handlers absent volume regulation. However, no such panic has been observed in periods of navel orange prorate suspension or in the sale of unregulated crops.

costs, the argument goes, would tend to result in an increase in the quantity supplied at a given price.26/

This argument does not withstand analysis, however. First, prorate may produce its own destabilizing effect on the navel orange market. In unregulated industries, retailers can be assured of supplies and handlers can be assured of outlets for their products because handlers can agree to deliver specified quantities at specified times in the future (forward contracts).27/ Yet, forward contracts and the assurances they provide are undermined by prorate. Under volume regulation, handlers do not know what they will be allowed to ship and cannot promise future delivery in all instances to retailers.28/ The uncertainty about timing and implementation of quantity controls introduces "regulatory risk" to navel

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26/ USDA has asserted, in enacting the 1990-91 navel orange Final Rule on December 5, 1990, that "there is a strong argument that prorates reduce variability in prices on an interseasonal basis, resulting in a rightward shift in the supply curve due to decreased producer uncertainty. That is, with decreased price variability, producers are willing to supply more oranges for a given return, resulting in an increase in social welfare." 55 Fed. Reg. at 50162. This assertion was unsupported by any evidence.

27/ Forward contracts are agreements between a grower and a buyer in which a price is set well in advance of the harvest. Such contracts enable growers to transfer the risk of low prices at harvest time to the buyer.

28/ Thus, NOAC's recommendation for volume regulation undermines the ability of handlers to assure supplies to retailers, even as NOAC concedes the importance of such assurances. Policy Statement, at 17.

orange markets that interferes with efficient marketing and investment decisions.

Moreover, while it is clear that prices to growers vary, it does not appear that navel orange growers face unusual price risks. Patterns of price variation often are associated with known seasonal patterns of changes in supply and demand, as well as with unexpected events such as unusually large crops attributable to good weather or lean crops resulting from a disastrous freeze such as occurred in 1990. Since weather is variable, yields per acre are variable and any year's harvest can produce relatively high or low prices.29/ The relevant question is whether prices and yields over the life of a tree vary significantly from what the grower expected when the tree was planted. Over the life of a tree, many small fluctuations will cancel each other out, so the relevant revenue is more stable than analysis of a single year would suggest.

Predictable seasonal variations do not constitute "risks," however, precisely because they are expected. Not only does any attempt to "stabilize prices" by counteracting predictable seasonal patterns in supply and demand not reduce risk, such

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29/ The fact that prices were relatively high in one year does not mean that more of the product could have been produced profitably in that year. Moreover, it is efficient for prices to rise during seasonal periods of high demand so that the existing crop is efficiently allocated among consumers.

attempts reduce social welfare by interfering with the efficient working of the price system.30/

Furthermore, while there is some uncertainty faced by navel orange growers even over the life of a tree, there is no evidence that these relatively minor variations are larger than risks successfully handled in other markets. Indeed, the NOAC Policy Statement (at 9) declares that the navel orange industry is "in good health" despite last year's freeze. Yet the Policy Statement also shows that the freeze created an extreme supply shock, and caused a huge financial loss for the industry. Production in the 1990-91 season was only 32,895 carloads, or about one-third of the 1989-90 level.31/ Though prices in the 1990-91 season were about 50 percent higher than in the 1989-90 season,32/revenue equalled only half that of the 1989-90 season. An industry that remains in good health after a loss of this magnitude is unlikely to be harmed by any minor price variations that might occur if prorate were not reinstituted in the current season.

Risks are not unique to the production of navel oranges and there are many ways that risk is handled in unregulated

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30/ It is efficient for prices to rise during seasonal periods of high demand so that the existing crop is efficiently allocated among consumers.

31/ See Table E.

32/ See Table 5.

markets.33/ Because the constraints of prorate interfere with some of these methods (e.g., forward contracting), prorate can lead to a net increase in price risk compared to an unregulated market with free use of forward contracts and other free market methods of handling risk. Indeed, in many comparable commodities, such market-based mechanisms are used successfully to reduce risks. Among these mechanisms are risk-reducing pricing methods such as pre-shipment pricing34/ and forward contracting, use of risk sharing organizations such as cooperatives and participation plans35/, diversification of

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33/ In adopting the Final Rule on volume regulation for navel oranges in the 1990-91 season, USDA dismissed these mechanisms out of hand as not meeting "marketing risks" to producers and handlers. These "marketing risks" were not identified and we are not aware of any that are not a normal part of similar businesses.

34/ Most navel orange sales today are made at firm prices before shipping. This is in contrast to earlier times when auction markets were the prevailing method of selling citrus. In those markets, sellers risked unexpectedly low prices because they would have to pick the fruit and transport it to the auction before they knew the selling price.

35/ Cooperatives take fruit produced by its members and pool it. A grower's proceeds depend on the average price received by the cooperative and are proportionate to the amount of fruit that grower contributed to the pool. A participation plan is an agreement between growers and handlers which pools the products of many growers and returns to the grower the average price received for the pool. These systems reduce the risk associated with daily price fluctuations since each grower in a given pool receives the same average price.

crops or income sources, better use of preservation and storage techniques, and increased access to market information.36/

E. The Net Effect of Prorate Is Negative

Evaluating whether price stablilization or other alleged effects of prorate have a net beneficial economic impact first requires establishing that there are stabilizing effects produced by prorate that outweigh any destabilizing effects from the creation of "regulatory risk" or interference with the market-based methods of handling risk described above. If there is a net price stabilization benefit, the costs of reduced navel orange consumption and resource misallocation must be balanced against any benefits of increased supply occasioned by greater price stability. A 1981 USDA report points to two criteria for evaluating the net economic impact:

> Continual use of [prorate] provisions, particularly use during years with average or smaller than average crops, or increasing diversion to secondary markets, would suggest that efficiency losses from misallocation are likely to exceed any stabilization benefits.37/

36/ Some form of regulation might arguably be justified if the market failed to provide sufficient information and opportunity to enable each participant to make an informed judgment about risk. Today, however, current market information is readily available and rapidly disseminated in the citrus industry, both through government and private publications and through the activities of cooperatives. With access to such information, growers, handlers and buyers can adapt to risk by adjusting their behavior quickly in response to changes in market conditions.

37/ USDA, A Review of Federal Marketing Orders for Fruits, Vegetables, and Specialty Crops 34 (1981).

Under both these tests, the net effect of navel orange prorate is likely to be negative. First, navel orange prorates have been used in almost every year since the order was authorized in the early 1950s, whether the crop was lean or full and despite significant variation in the size of the crops. Second, as detailed above, the portion of the crop that is diverted to secondary markets has grown from about 7 percent in 1960 to about 25 percent in the 1980s.

During the 1980s, the California-Arizona navel orange prorate was suspended for part of the season a number of times. USDA has produced two studies, one in 1986 and the other is 1990, in which the authors examined the effects of these suspensions.38/ Both concluded that economic welfare increased when prorate was suspended.

The 1986 USDA study projected (based on 1984-85 data) that a season-long suspension would lead to an increase in the shipments of fresh navels, with a corresponding decrease in the shipments of processed navels. The study predicted that prices

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38/ N. Powers, G. Zepp & F. Hoff, supra, n. 16; N. Powers, supra, n. 24. The first study focused on the suspension during the 1984-85 season that took effect after 52 percent of the crop had been marketed. The second study examined all navel orange prorate suspensions during the 1980s through the 1988-89 season.

of fresh navels would drop, the prices of processed navels would remain unchanged, and economic welfare would increase.

The 1990 study also showed that the quantity of fresh navel oranges consumed increased and the consumption of processed navels decreased as a result of prorate suspension during portions of each of the growing seasons from 1982-83 to 1988-89. These changes led to a decrease in the price of fresh navels and an increase in the price of processed navels. The study estimated social gains attributable to suspensions ranging from $4.4 million in 1982-83, a large crop year, in which there were small shipments during suspension, to $43.5 million in 1984-85, a small crop year, in which there were large shipments during the suspension.

The destructive effects of the December 1990 freeze, discussed at length in the NOAC Policy Statement, provide dramatic evidence of the harmful effects of prorate. Volume regulation in the 1990-91 season lasted for only four weeks before the freeze hit. On January 9, 1991 USDA, recognizing the severe damage that had been done, suspended volume regulation for the 1990-91 season. 56 Fed. Reg. 774. Yet, in the period while prorate was in effect, some navel oranges that would have been available to an unregulated market could not legally be sold. Thus, the losses unavoidably caused by the freeze were magnified by unnecessary regulation. NOAC's Policy Statement notes (at 2) that in enacting the AMAA Congress expressed concern about impairment of the purchasing power of farmers and destruction of the value of agricultural assets. To the extent that additional impairment of purchasing power and destruction of agricultural assets accrued because of governmental prorate action, the intent of Congress in enacting the AMAA has been frustrated.

In contrast to the persuasive empirical evidence that exists as to the harm of prorate, NOAC has offered only conclusory assertions of benefits. NOAC's Policy Statement lists benefits that the Committee believes have accrued to the navel orange industry as a result of the Order such as an expanded marketing season, development of a cold protection system, and introduction of new navel cultivars. (Policy Statement, at 19). Many similar benefits, however, have been achieved in the marketing of other crops without regulation and NOAC offers no explanation why technological advances would not occur but for volume regulation.

NOAC further suggests that without prorate there would be a "helter-skelter" rush to sell fruit that is not at optimum maturity. Policy Statement at 22. This argument is without merit. First, the ability to store oranges on the tree provides handlers with no incentive to sell less than optimum quality fruit. Second, the argument implicitly suggests that fruit that is unregulated is sold in bad condition. Such a suggestion is unsupported by evidence. Retailers are unlikely to deal with handlers who provide fruit that consumers do not like. Consequently, protection of their own long-term interest, if nothing else, dictates that handlers refrain from rushing immature fruit to market.

In adopting the final rule on volume regulation for navel oranges for the 1990-91 season, USDA based its conclusion first on the mistaken presumption that the government should regulate absent proof that it should not, and then on a perceived evidentiary void: "There is no evidence that, in the absence of flow-to-market controls, a price depressing surplus of shipments would be any less likely now than it was four decades ago." 55 Fed. Reg. 50163. The presumption should be to rely on competition absent evidence of significant market failure that is not adequately resolved by methods short of regulation.39/ No such market failure has been shown to exist at this time with respect to navel oranges. As we have discussed above, and as NOAC concedes, marketing by producers and handlers in the industry has become far more sophisticated since the Order was put in place in 1953. More importantly, the Department of Justice has provided relevant evidence to predict the likely net effect of prorate, and to quantify its harm. That evidence leads to the firm conclusion that the 1991-92 season is an ideal time to allow the market to work.

39/ See generally, "Regulatory Impact Analysis Guide," reprinted in Regulatory Problems of the United States Government, Appendix V.

CONCLUSION

Imposition of prorate in the 1991-92 navel orange season, especially in view of the small size of the projected crop and the absence of evidence indicating that suspension of prorate has resulted in disorderly marketing conditions, is unwarranted. The Secretary should exercise his discretion and allow the market to operate without volume restrictions.

Respectfully submitted,

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